THE COMMONWEALTH OF MASSACHUSETTS
EXECUTIVE OFFICE FOR
ADMINISTRATION AND FINANCE
STATE HOUSE ▪ ROOM 373 BOSTON, MA 02133

Meeting Minutes

Debt Affordability Committee
December 9, 2022
1:00 pm
Executive Office for Administration and Finance
Zoom URL: https://mass-gov-anf.zoom.us/j/88490960878?pwd=T0dVTmQ4a1A5RDRVWkZxckRpMjY2dz09
Password: DAC120922
Teleconference line: *713-353-7024*; Conference code: 319738

A meeting of the Debt Affordability Committee was held on December 9, 2022. In accordance with Section 20 of Chapter 20 of the Acts of 2021, as extended by Chapter 107 of the Acts of 2022, this meeting will be conducted, and open to the public, via Zoom and Teleconference.

Minutes:
The meeting was called to order at 1:01 pm.

Board members comprising a quorum:

Kaitlyn Connors, Chair, Executive Office for Administration & Finance
Navjeet Bal, Appointee of the Treasurer
Martin Benison, Appointee of the Treasurer
Michelle Ho, Massachusetts Department of Transportation
Pauline Lieu, Office of the Comptroller
Susan Perez, Office of the Treasurer and Receiver-General
Catherine Walsh, Designee for Governor Baker

Others in attendance:

Representative Danielle Gregoire
Patrick Walsh, Representative Gregoire's Office
Timur Kaya Yontar, Executive Office for Administration and Finance (Capital Director)

Minutes:

Ms. Connors called the meeting to order and conducted the roll call for attendance.

Minutes from the December 2, 2022, meeting were not ready. Ms. Connors proposed that the Committee meet again on Wednesday, December 14, at 2pm, to adopt those minutes, since they reflect the vote from December 2 on the Committee's recommendation to the Governor. Members agreed with her proposal.

Ms. Connors then proceeded to the next item on the agenda, a review of the slide deck that comprises the main discussion points of this year's Committee meetings and that will accompany the recommendation to the Governor. The deck comprises three sections and she proposed that the Committee briefly review the first section on the FY2024 Recommendation, not review the second section on background reference materials in great detail given these were slides the Committee has reviewed multiple times, and spend most of the meeting reviewing the third section in more depth which is the new, one-time report to the Legislature on Reducing Debt Service Costs and Improving Credit Ratings.

Ms. Connors explained that Section One provides a summary of the Debt Affordability Committee's roles and responsibilities. Ms. Bal recommended that a bullet on the new statutory reporting requirement be added to the DAC introduction. Ms. Connors agreed it made sense to include a bullet on the new requirement upfront and said she would include it in the final report, noting that the requirement is one time in nature and the reference would likely need to be removed by the Committee next year. Ms. Connors then proceeded to review the next sections of the report which included an overview of the statutory and administrative limits on direct, factors the DAC uses to inform its recommendation, and the Committee's workplan, noting that an additional meeting will be held on Wednesday, December 14, 2022 at 2pm.

Ms. Connors then proceeded to review the next sections of the report and noted that slides presented in these sections are the same slides the Committee had reviewed in priors meetings, starting with the modeling slides that show the modeling outcomes of the DAC recommended $125 million bond cap increase, as well as alternative scenarios considered, and then moving through the slides that focus on modeling assumptions details (revenue growth and interest rate assumptions), credit factors which include key debt ratio metrics and state comparisons, and an overview of the Commonwealth's current debt portfolio.

After the review of the slides, committee members offered a number of suggestions and points of feedback. Ms. Bal recommended that the slide on Moody's current projections include an "as-of" date. Ms. Lieu noted that the description of general obligation debt on the Commonwealth Outstanding Debt slide does not seem to be sufficiently descriptive. Ms. Perez recommended that reference to gas tax bonds be removed since the bonds have been paid off. She also pointed out that the S&P rating on the Convention Center was increased to A- and should be updated in the report. Ms. Perez also suggested that the revenue slides indicate that the data included in the Committee's final report s from the Department of Revenue's October presentation which was used to inform the Committee's modeling which began at that time (October). Ms. Connors agreed with the suggestion, noting that the revenue data was the most available information the Committee had at the time it began modeling. Ms. Perez also said she would send Ms. Connors proposed edits to several pages via email.

Ms. Bal mentioned she had sent several comments via email as well. She mentioned most comments seemed to have been incorporated, however she had provided feedback on the Committee Consideration slides, at the beginning of the deck, which had not been address – including a reference to comparisons to New England states and some others states that seem as though they may be outdated. Ms. Connors said she would go back and look at the comments and make sure the feedback is incorporated appropriately. Ms. Connors asked if there were any other questions related to the sections the committee reviewed; there were none.

Ms. Connors then began reviewing the last section of the report which addresses the new DAC reporting requirement. She reviewed the statutory language and then summarized the Committee's agreed upon approach: the Committee would provide a fact-based, high-level discussion of two report topics (measures to reduce debt service and measures to improve credit ratings). However, the Committee is not endorsing any one of these measures and acknowledges that there are policy trade-offs and considerations that policy makers will have to evaluate in much greater detail should they be further explored.

Ms. Perez offered minor edits to the wording of the slides on the Committee's approach to the new reporting requirement. Mr. Benison acknowledged that he liked the approach and acknowledged that the Governor and the Legislature have a lot of considerations on what they fund and don't fund and what revenue they increase or do not increase and believes this approach and slide captures this.

Ms. Connors then moved on to talk about reducing debt service. She noted that once bonds are issued, debt service is fixed and cannot be changed. Refunding opportunities (to take advantage of a lower interest rate environment) are limited and driven by financial markets and that refunding savings are typically realized in equal amounts over the life of the refunded bonds (on average over 20 years). She also highlighted the fact that the Treasurer's Office actively manages the debt portfolio and takes advantage of savings opportunities as they arise and that over the past 10 years, key debt service metrics have been improving. She then walked through the key improvements in debt per capita, debt to personal income, and debt service as a percentage of expenditures that have occurred since 2011. She noted that the last two points are based on feedback from the

Committee last week and asked if Committee members had any additional thoughts or concerns. Ms. Lieu stated she liked the additional tables that were included. Ms. Perez offered edits to the slides to soften some langue around limited opportunities and removed reference to interest savings.

Ms. Connors then moved on to discuss strategies for thinking about reducing future debt costs. She explained the cost of debt service is driven by the amount of bonds issued and the interest rates at the time of issuance. The amount of bonds issued is based on the approved Capital Improvement Plan (CIP), which is guided by the DAC recommendation on how much debt can prudently be afforded by the Commonwealth each year. In general, if the Commonwealth would like to limit relative debt service costs going forward, it would need to issue relatively less debt.

Ms. Connors asked if the Committee had any questions or comments and Ms. Perez suggested that Ms. Connors add a reference to finding additional funds for CIP in addition to issuing less debt. Ms. Lieu then asked about the debt reduction and liabilities fund. Ms. Connors and Ms. Perez both acknowledged that this fund exists and that it is used to help reduce debt service should an opportunity arise. Ms. Perez noted it is funded with excess gaming revenues and that it is a relatively small amount. There were no other questions.

Ms. Connors then began reviewing the slides that related to improving credit ratings. She reviewed recent credit agency feedback and scoring and noted that the Commonwealth receives high scores from all the credit rating agencies in most areas, except long-term debt and liabilities. She then reviewed the Commonwealth's overall long-term debt liabilities since 2011 and noted that long term liabilities as a percentage of expenditures has remained relatively flat.

Next, Ms. Connors walked the Committee through Commonwealth credit strengths, recognizing current credit strengths offset the Commonwealth's high debt burden and play a key role in maintaining current ratings. A ratings increase would not be possible if these strengths diminished. Key strengths include strong reserves, high income levels, and a diverse and resilient and economy. Ms. Connors then reviewed the credit offsets in more detail. She noted that the Commonwealth has taken a number of steps to strengthen its pension system including: increasing its contributions as a percentage of its ARC since 2017, increasing its annual pension contributions by 9.63% to fully amortize unfunded liabilities by FY 2036 (in advance of the requirement to fully fund by FY 2040) and utilized budget surplus to make supplemental transfers to the pension fund fiscal years 2022 and 2023. And she noted.

Ms. Lieu noted that PERAC recently updated its valuation. Ms. Connors said she would use PERAC's most recent numbers. Ms. Perez asked if the Committee should acknowledge Commonwealth's fiscal discipline around pension. Ms. Ho agreed and offered suggested language. Ms. Connors then touched on OPEB, noting progress has been made in recent years.

Ms. Connors then moved on to discuss how the Commonwealth compares to other states, noting MA ranks 3rd in terms of state with the highest debt per capita, however the Commonwealth makes substantial payments to cities, towns, and school districts and services which in other states are funded at the local level. When looking at combined state and local debt, Massachusetts debt levels are moderated.

Ms. Connors then reviewed the potential measures for improving credit ratings that the Committee had agreed upon in previous meetings. She noted that most of the material has not changed although the Committee's feedback from the last meeting has been incorporated. The first potential measure is limit future general obligation debt by **reducing future annual capital budgets** which could entail decreasing investment in state owned facilities and infrastructure or decreasing investment in community grant programs funded through the CIP. The policy considerations associated with each did not substantially change from the prior week. Decreases in CIP funding for state-owned assets could have negative consequences, which could be further compounded when considering future inflation:

(1) Increased backlog of deferred maintenance and increased costs due to lack of preventative

maintenance and emergency repairs
(2) Outdated facilities that do not meet the needs of those who work or receive services there
(3) Increased vulnerabilities/risk related to climate change and or risk of not meeting environmental targets for reducing green house gases (GHG)

Ms. Connors also noted that the Commonwealth could consider reducing the amount of debt it issues to support programs directly benefiting local communities, although policy makers will need to determine whether the potential benefits of reducing debt outweigh the potential hardship this may cause communities and/or loss of economic benefits those investments generate, and whether certain communities are impacted disproportionately. Ms. Bal suggested the report be more explicit in referencing impact on economically disadvantaged communities being disproportionately impacted. Ms. Perez agreed.

Ms. Connors then moved onto the next potential strategy for limit future debt: identify other non-bond cap funding sources to support capital which could include operating or federal funds. Ms. Connors noted the policy consideration now includes reference to the fact that debt financing helps spread the cost of capital to users over the life of the asset, helping to ensure that those who are paying are those who can/are benefitting from the infrastructure. Using operating revenues to fund assets with longer useful lives is less effective at spreading costs out to current and future users. Ms. Connors also noted that federal funds would likely require a higher upfront state match but may ultimately reduce future capital costs. She also noted that the current CIP includes increased federal funding from BI/IIJA. Ms. Connors asked the Committee if they had any feedback. Mr. Benison, Ms. Bal, and Ms. Ho offered feedback on the language to use. Ms. Ho pointed out that the state match will depend on the grant.

Ms. Connors then noted that the report now includes a discussion on special obligation bonds as a potential revenue option. Ms. Perez suggested that special obligation bonds be split into 2 categories: 1. increasing capacity under existing special obligation debt by identifying and or increasing pledged revenue streams and 2. exploring the possibility of establishing other special obligation credits, which would involve pledging specific revenue streams for capital. In either case, the Commonwealth would need to evaluate the trade-offs associated with pledging specific revenue streams that could be used for other purposes.

Ms. Connors then turned to the last section of the report which discussed potential measure 2: reducing unfunded pension and OPEB liabilities. Potential strategies include: (1) continuing to increase annual pension contributions to fully amortize unfunded liabilities by FY 2036 (per schedule); (2) continuing to maintain state finance law requiring 5% of capital gains income to be transferred into each of the Pension Liability Fund and State Retiree Benefits Trust Fund (i.e. do not suspend law) and (3) appropriating budget surplus (when available) to pension & OPEB funds. Mr. Benison noted that the Commonwealth has incurred the obligation and the policy choice is not whether to fund it, but whether to fund it now or later. Ms. Bal, Ms. Perez, and Ms. Ho and Ms. Walsh agreed. Mr. Benison also noted the Committee may want to consider saying something about committing to an OPEB schedule.

Ms. Connors asked whether there were any other questions or feedback. There was none. Ms. Connors indicated that she would make the edits and seek approval of the revised deck at the next meeting.

With no further business, the meeting was formally adjourned at 2:01 pm.

The next DAC meeting is scheduled for Wednesday, December 14th, 2022, at 2:00 pm.